U.S. GENERAL SERVICES ADMINISTRATION
Office of Inspector General

OCT 21 2009

MEMORANDUM FOR PAUL F. PROUTY
ACTING ADMINISTRATOR (A)

FROM: BRIAN D. MILLER
INSPECTOR GENERAL (J)

SUBJECT: GSA's Major Challenges

Attached is a copy of our office's updated assessment of the major challenges currently facing GSA. The Reports Consolidation Act of 2000, Public Law 106-531, requires that each Office of Inspector General (OIG) prepare a statement that summarizes what the Inspector General considers to be the most significant management and performance challenges facing the agency and briefly assesses the agency's progress in addressing those challenges.

We are hereby providing you with our assessment to afford you the opportunity to review and prepare any comments you wish to append.

If you have any questions or wish to discuss this, please call me at 202-501-0450. If your staff needs any additional information, they may contact Theodore R. Stehney, Assistant Inspector General for Auditing, at 202-501-0374.

Attachment

1800 F Street, NW, Washington, DC 20405-0002

OFFICE OF INSPECTOR GENERAL'S ASSESSMENT OF GSA'S MAJOR MANAGEMENT CHALLENGES

OCTOBER 2009

As required by the Reports Consolidation Act of 2000, the Office of Inspector General (OIG) regularly identifies what it considers the U.S. General Services Administration's (GSA) most significant management challenges. This effort highlights the Agency's most demanding issue areas. Some challenges represent an inherent risk to GSA's mission or programs and not necessarily a deficiency in performance. As such, GSA management may not be able to eliminate some challenges, but should continue to take steps to mitigate these challenges.

The following represent the most serious challenges facing GSA: Acquisition Programs, Financial Reporting, Information Technology, Human Capital, Protection of Federal Facilities and Personnel and the Federal Buildings Fund (FBF).

ACQUISITION PROGRAMS

We have identified the following two issues: (1) pricing and compliance under the Multiple Award Schedules (MAS) program; and (2) the timely transition from the FTS2001 and Crossover contracts to the Networx contracts.

ISSUE: Challenges exist in the Multiple Awards Schedules program pertaining to pricing and compliance. Under the MAS program, GSA's Federal Acquisition Service (FAS) establishes long-term government-wide contracts with vendors to provide federal agencies access to over 11 million commercial supplies and services. GSA negotiates the contracts with the objective of achieving the vendors' most favored customer (MFC) pricing/discounts under similar conditions. Federal agencies then simply order supplies or services from the schedules at the pre-negotiated prices and pay the contractors directly for their purchases. Schedule sales for FY 2008 totaled approximately $38 billion. It is anticipated that with the enactment of the American Recovery and Reinvestment Act (Recovery Act) of 2009, additional sales may be generated through the MAS program.

Pricing

The OIG is concerned that, with the growth of the MAS program, the emphasis of certain program fundamentals, including pricing objectives and other pricing tools, has diminished. These fundamentals, which are set by regulation, include the mandate to seek the offeror's best price. These fundamentals, which are set by regulation, include the mandate to seek the offeror's best price (MFC pricing), the requirement to perform meaningful price and cost analysis when awarding or extending contracts, and the use of field pricing assistance to assist in negotiating contracts. MFC pricing ensures that MAS contract pricing harnesses the federal government's collective buying power for pricing purposes. Price analysis is the key substantive step a contracting officer performs for the purpose of arriving at fair and reasonable prices. We have reported that contracting officials were not consistently negotiating MFC prices; many MAS contract extensions were accomplished without adequate price analysis; and available tools were not being used effectively to negotiate better MAS prices. Additionally, we have found that vendors can go to great lengths to misrepresent their actual selling prices.

Pre-award reviews are the main tool by which a contracting officer can be assured that a vendor's pricing is appropriate. Such reviews also provide contracting officers with additional details regarding a vendor's pricing and sales practices in anticipation of negotiations. During FY 2007 and FY 2008, the OIG found flaws in many of the proposals audited that amounted to over $1.4 billion in proposed contract price reductions and tens of millions of dollars in recoveries.

In addition, the broad scope of the Federal Acquisition Regulation (FAR) definition of a commercial item affects issues with pricing. Under the current definition, a commercial item is any item and many services "of a type" customarily used by the general public. Thus, the current FAR definition of a commercial item does not require a vendor to have any commercial, competitive sales of a product or service. The MAS program operates under the premise that: (1) GSA vendors would routinely sell their commercial products and services to the general public in a competitive open market; (2) this competitive process would establish "market prices" (fair and reasonable prices); and (3) GSA contracting officers could use market prices as a starting point in negotiations to establish a government price that was equal to a like buyer in the private sector. Based on this expanded definition of a commercial item, it has been our experience that many MAS vendors have only federal government sales. There are also vendors who create a corporate structure to organizationally segregate their commercial business from their government business. In addition, we have found that, although a commercial market exists for a vendor's services, its commercial contracts are typically awarded on a firm fixed price basis, while its GSA schedule clients have been mainly doing business on a time and materials basis. All of these scenarios present difficult challenges in terms of comparability, and impact a contracting officer's ability to perform valid price analysis.

<u>Contract Compliance</u>

The OIG is concerned that MAS vendors are not fully in compliance with the terms and conditions of their contracts. We have previously reported to the MAS Advisory Panel that 70 percent of Commercial Sales Practice data provided by vendors was not current, accurate, or complete. In addition, GSA was not offered MFC pricing, the target of all contract negotiations, a majority of the time. To provide an example, in April 2009, a MAS vendor agreed to pay the United States government $128 million to resolve alleged false claims and contract fraud. This vendor knowingly failed to comply with the price reduction clauses of its GSA contract by failing to disclose to GSA discounts the vendor gave to its commercial customers, which were higher than the discounts that had been disclosed to GSA.

AGENCY ACTIONS: There is an on-going program for pre-negotiation clearances to ensure the quality of its most significant contract negotiations. In this process, the contracting officer presents a summary of his or her actions in developing negotiation objectives including market research, contractor responsibilities, and price analysis to a panel for evaluation. Also, there are several initiatives that may have an effect on the program in FY 2010. FAS established an office in September 2008 to develop and implement consistent acquisition policy and guidance for the MAS program that is currently housed under several different offices within FAS. In addition, FAS is using Lean Six Sigma in evaluating its contracting process, emphasizing process efficiency and effectiveness.

ISSUE: GSA needs to ensure agencies transition to Networx in a timely manner. The transition of government agencies from the FTS2001 and Crossover contracts to the Networx contracts, Universal and Enterprise, is one of the largest telecommunications services transition ever undertaken by the federal government. It will involve more than 135 agencies, more than 50 services and thousands of voice and data circuits. The Networx contracts are valued at $68.2 billion, divided between Networx Universal and Networx Enterprise.

In May 2009 meetings, management stated they are on target with regard to budgeting; however, progress with accelerating agencies' transition still needs to be made. As of August 2009, GSA officials stated that over half of the contractor selections had been made. The transition will require coordination between agencies, GSA, and a host of telecommunications contractors.

AGENCY ACTIONS: In an effort to decrease the immediate transition burden on agencies migrating from the existing FTS2001 contracts, GSA awarded bridge contracts that provide for continued service beyond the expiration of FTS2001 in 2006 and 2007. The bridge/Crossover contracts are set to expire in May and June 2010; however, continuity-of-service contract provisions allow the contracts to be extended until May/June 2011.

FINANCIAL REPORTING

ISSUE: Financial management systems, internal controls, and financial reporting need improvement. Each year since FY 2004, the Independent Public Accountant has reported deficiencies surrounding GSA's financial management systems, its processes and substantial transaction errors resulting from insufficient controls related to reporting of budgetary accounts and balances. The Independent Public Accountant emphasized that the root cause of these weaknesses primarily points to the Agency's business feeder systems and management's reliance on costly compensating processes. However, GSA systems, including its financial system of record, Pegasys, continue to have deficiencies in interoperability and interfaces. As a consequence, GSA management continues to rely heavily on manual workarounds and significant adjusting entries to prepare the financial statements and related note disclosures. Specifically, one of GSA's major feeder systems, Comprizon, does not interface with Pegasys or any other financial management system; therefore, contracts entered into the feeder system must be manually entered into Pegasys and cumbersome worksheet adjustments need to be made to prepare the financial statements and related note disclosures.

AGENCY ACTIONS: Management is continuing its efforts to work with the regions to instruct them on the importance of having valid transactions for the programs as well as for financial reporting purposes. Also, the Office of the Chief Financial Officer (OCFO) is continuing to instruct the regions on how to properly account for contracts as well as timely recording of obligations.

The OCFO is requiring regional and program offices to proactively check the status of outstanding budgetary transactions and take appropriate actions as necessary. In addition, the OCFO is taking steps to help the regions and program offices identify high risk populations for self review of potential invalid transactions.

INFORMATION TECHNOLOGY

We have identified three issues in regard to Information Technology (IT): the need for improved planning, development and implementation of IT systems; the need for improvements in GSA's IT Security Program; and, the need for increased contract oversight and coordination of managed service offerings and lines of business.

ISSUE: Improved planning, development and implementation of IT systems are needed to support GSA missions, programs and implementation of the Recovery Act. Planning, developing, and implementing cost-effective, customer-focused, and performance-based IT systems in support of GSA's strategic business goals and various missions are keystones to good business. The Chief Information Officer (CIO) has stated that providing effective and reliable IT systems and solutions and providing balanced stewardship of information and technology are key Agency-wide IT strategic goals that also relate to supporting GSA's implementation of the Recovery Act. GSA management faces challenges in meeting these two goals. For example, GSA systems often do not meet standards for interoperability and interfaces, resulting in duplication of business processes, cost inefficiencies and customer dissatisfaction. Challenges in reengineering business processes across the Agency and implementing an enterprise architecture have led to multiple, duplicative systems that are costly to maintain and operate. As an example, common services and integrated information systems have not been developed in support of GSA's acquisition business processes. Duplicative business processes and systems will make it difficult for the Agency to track and report management information needed to make strategic system decisions and support the Recovery Act.

AGENCY ACTIONS:

- To guide IT investment decisions and communicate long-term goals and objectives, the GSA CIO has developed an IT Strategic Business Plan covering FY 2010 – 2012. The plan is intended to enable the planning, decision making, acquisition and execution of IT services by, individual Services/Staff Offices and business-level program areas.

- As detailed in CIO Order 2130.1, "GSA Information Technology Governance," November 26, 2008, the GSA CIO has updated agency-wide governance processes for IT to reduce inconsistency and redundancies in responsibilities and processes for IT management. Specifically, GSA has established an IT Executive Council (ITEC) that reviews and makes decisions and recommendations on the strategic use of IT. The ITEC oversees five standing committees in GSA, including one for enterprise applications, enterprise architecture, information security, portfolio management and enterprise infrastructure.

- GSA Services and Staff Offices have requested funding for new IT programs and initiatives, as part of the Agency's FY 2010 Budget. These new IT programs and initiatives seek to better manage GSA's legacy systems environment. Examples are:

    - GSA requested approximately $49 million for the acquisition and development of a new BAAR solution, to be incrementally phased in by business lines. This is expected to reduce the need for manual reconciliation and consolidate multiple financial applications within GSA's financial management enterprise architecture.

    - Public Buildings Service (PBS), E-Gov initiatives. The PBS CIO requested funds in the amount of $6.5 million; $3.56 million for the System for Tracking and Administering Real Property (STAR) replacement; $1.5 million for a Pegasys-Comprizon interface; and $1.5 million to implement the BAAR solution.

    - FAS Information Technology Services Fund. FAS requested funding to replace FSS-19 to mitigate risks with this legacy system, as the U.S. Department of Defense (DoD) is in the process of updating its systems and FAS must keep pace in order to continue serving DoD. Also, funding was requested for the Regional Telecommunications program, which will be undertaking a significant transformation by moving from owned private branch exchange (PBX) switches to common infrastructure, such as voice over internet protocol or broadband technologies.

ISSUE: Improvements are needed in GSA's IT Security Program to protect sensitive Agency information and address emerging risks. Improved processes and controls to address evolving IT security risks and requirements established with the Federal Information Security Management Act of 2002 (FISMA) pose long-term challenges for GSA leadership. Ensuring that system security officials comprehensively evaluate risks and implement necessary controls for GSA IT systems through the Agency's certification and accreditation process remains a key challenge for GSA's IT Security program. Specifically, the certification and accreditation process often is not providing senior Agency management with the information they need to make risk-based decisions about the IT systems for which they are responsible. Further, programmatic improvements are needed to ensure the integration of critical information security activities into the systems development processes. For example, coordination, collaboration and accountability across the Agency is needed to address high priority risk areas related to (1) access controls, (2) oversight of contractor supported systems and (3) controls for sensitive data. This would help to reduce costly security enhancements/modifications that need to be made to GSA systems to address security control weaknesses once implementation has occurred. At the same time GSA is seeking to improve its security program, it is also pursuing innovative solutions to other issues that introduce new risks. GSA is evaluating the use of cloud computing technologies in the Agency and recently launched an online storefront offering cloud computing services to federal agencies. With "cloud computing", traditional system boundaries and definitions may no longer apply. Moreover, existing policy frameworks and governance processes may need to be strengthened to ensure that sensitive information is secured and the privacy of American citizens is maintained in the "cloud."

Several key systems at GSA are provided under managed service offerings, so adequate oversight from GSA's IT Security program is critical to ensure that security requirements are met for these systems. In addition to using these systems for internal agency needs, GSA provides these systems to several other federal organizations. As such, ensuring that roles and responsibilities are clearly established for meeting security requirements is a key risk area that GSA's IT Security program should address. A risk-based approach that ensures continuous monitoring processes are implemented and that in-house and contractor operated systems and services meet federal and Agency security requirements is needed. Development and implementation of adequate management, operational and technical controls to: (1) prevent the loss of or unauthorized access to, sensitive data; (2) detect unauthorized disclosures or IT security breaches; and (3) recover or restore systems and data remains a significant challenge for GSA's Privacy and IT Security programs.

AGENCY ACTIONS:

- GSA has formed the Information Assurance Committee (IAC) to oversee the development and implementation of the Agency's security policy. The IAC is chaired by the Senior Agency Information Security Official and the Chief Privacy Officer. Further, a subcommittee to address weaknesses in access controls across the Agency has been established under the IAC. This subcommittee includes representatives from GSA Services, Staff Offices and Regions.

- In July 2009, the GSA CIO updated agency-wide IT Security Policy to address changing risks and requirements for GSA systems.

- In response to audit findings and other identified risks, the GSA CIO updated several guides covering such areas as certification and accreditation, software configuration, and rules of behavior.

- GSA piloted the use of HSPD-12 cards for access to information systems in several regions. GSA plans to utilize HSPD-12 cards to improve access controls for Agency information systems.

- To make Agency operations more transparent, collaborative and participative, GSA has been implementing social media technologies, such as blogs and wikis. The GSA CIO recently issued policy and procedures for security of these emerging technologies.

- GSA is leading efforts to assess the use of cloud computing technologies for the government. As part of this effort, GSA is working on developing security requirements and has issued a Request for Information to the vendor community.

ISSUE: Increased contract oversight and coordination is needed for successful implementation of Managed Service Offerings and Lines of Business. As a managing partner for five E-Gov initiatives: Data.gov, E-Travel, GovSales.gov, Integrated Acquisition Environment and USA Services: and two lines of business, IT Infrastructure and Financial Management. GSA plays a leading role in improving IT for the federal government, citizens and businesses. As such, GSA is responsible for ensuring that these initiatives are cost effective, streamline government operations, increase efficiency and meet the needs of a diverse customer base. Success for GSA as a managing partner for these initiatives will require innovation and the ability to respond quickly to changing customer requirements and risks. A key risk for managed service offerings and lines of business is contract oversight to ensure that systems supporting these initiatives are developed, maintained, and operated in accordance with federal policies, standards and guidelines. Further, ensuring system usability and satisfaction remains a challenge to ensuring broad adoption of these initiatives.

AGENCY ACTIONS:

- As part of the FY 2010 Budget, GSA has requested $33 million for the Electronic Government Fund to: (1) address the areas of open government and transparency; (2) enhance citizen participation in government; (3) realize potential savings through alternative approaches to IT infrastructure; and (4) advance the use of innovative technology, including increasing agency use of collaborative technologies across the government.

- The IT Infrastructure Line of Business team is working with the Office of Management and Budget's (OMB) E-Gov and Budget offices to ensure consistency with related federal IT programs such as the Federal Enterprise Architecture Program Office, Strategic Sourcing and the Information Systems Security Line of Business. Additionally, this team is supporting government-wide cloud computing initiatives. As part of this effort, the team will assist with: developing a strategic approach for the federal cloud(s); addressing barriers and compliance issues; developing mechanisms to purchase infrastructure as a service; identifying and providing access to standard collaboration and communication tools, and allowing agencies to acquire cloud services as a commodity.

- The Financial Management Line of Business (FMLoB) team has published a final business process standards document for funds management, payment management and receivable management. The team is also working on several key initiatives including, updating, the Core Financial System Requirements and the Common Government-wide Accounting Classification (CGAC) structure to reflect the International Organization for Standardization (ISO) 9000 naming standards.

HUMAN CAPITAL

ISSUE: GSA faces challenges maintaining the workforce for future years. There are two components to the human capital management challenge facing GSA: succession management strategies to mitigate the risk of projected retirements of the leadership cadre and the critical gaps in acquisition workforce, particularly with the implementation of the Recovery Act.

<u>Succession Management Strategies</u>

Since 1998, the OIG has consistently cited human capital management as one of the major management challenges facing GSA that, if not addressed, will result in a loss of both knowledge and critical skills. In 2001, Government Accountability Office (GAO) added this to its high-risk series of issues facing federal agencies, and it continues as an issue on the January 2009 list.

As with many federal agencies, a large portion of GSA's acquisition staff has reached, or is nearing, retirement age. Workforce data indicates that approximately 33 percent of GSA acquisition employees will be eligible to retire within the next five years and approximately 40 percent will be eligible to retire within the next seven years. In addition, GSA's attrition rate stands at around eight percent, which is similar to that of the overall government. As a result, GSA needs to continue to attract new talent to fill the vacated positions. However, as noted by GAO, the current federal hiring process is often an impediment to the very customers it is designed to serve, in that it makes it difficult for agencies and managers to obtain the right people with the right skills, and applicants may become discouraged from entering public service because of the complex and lengthy procedures. Therefore, it is critical that GSA take action to: set the Agency apart as an employer of choice; improve the hiring process with regard to how long it takes to fill a position; and improve both the manager and the applicant experience.

Critical Gaps in the Acquisition Workforce

Another area of concern is the retention of a skilled acquisition workforce. Although the percentage of hires has increased, there remains a significant shortage of skilled acquisition professionals. GSA's acquisition workforce is integral to achieving its mission of leveraging the buying power of the federal government to acquire best value for taxpayers and our federal customers. Particularly with the implementation of the Recovery Act, GSA needs to ensure that there is a highly skilled cadre of acquisition professionals who can successfully function in a variety of acquisition positions. GSA's retirement projections, along with the current hiring and retention of skilled acquisition professionals, emphasize the need for an expedited recruitment process, succession planning and leadership development.

AGENCY ACTIONS: The U.S. Office of Personnel Management (OPM) and OMB partnered and launched a federal hiring reform initiative to address the need to improve the federal hiring process. In June 2009, OPM and OMB requested that agencies take steps to reform their hiring process. In direct response to the OPM and OMB mandate, GSA established a hiring reform SWAT team comprised of 20 hiring managers and nine Human Resources (HR) officials to work collaboratively as a Lean Hiring Team. This team will develop a process that results in hiring the absolute best candidates in the least amount of time and meeting all of the OPM action items.

GSA's "Lean Hiring" initiative focuses on specific actions that can be taken to improve the timeliness and quality of GSA's hiring process. Through "Lean Hiring", the Office of the Chief Human Capital Officer (OCHCO) is taking a critical look at HR service delivery in five key areas: policy, planning, systems, structure and processes. "Lean Hiring" will also help GSA develop a more systematic workforce planning process. In addition to "Lean Hiring", OCHCO also developed a succession plan that outlines strategies to address recruitment, retention and development of the acquisition workforce. The objective of the plan is to provide a clear and achievable strategy for employees to obtain the necessary skills to successfully advance to higher levels of authority in the acquisition field.

As of September 15, 2009, the regional General Management & Administration (GM&A) functions were transferred to Central Office. As part of this GM&A realignment, HR functions will be transferred from regions to OCHCO and a servicing HR unit will be established in each region.

PROTECTION OF FEDERAL FACILITIES AND PERSONNEL

ISSUE: Challenges exist concerning efforts to safeguard federal facility assets and provide a secure work environment for federal employees. Providing a safe, healthy and secure environment for over one million workers and visitors to approximately 8,600 owned and leased federal facilities nationwide is a major multifaceted responsibility of GSA. Increased risks from terrorism have greatly expanded the range of vulnerabilities traditionally faced by building operations personnel. Although the Federal Protective Service (FPS) was transferred from GSA's PBS to the U.S. Department of Homeland Security (DHS) in March of 2003, the Agency has a continual need to closely interact with security personnel due to GSA's mission of housing federal agencies. FPS is the primary agency responsible for providing protection to GSA buildings and facilities. Ensuring that federal employees have a secure work environment and that building assets are adequately safeguarded must remain a primary consideration for GSA.

GSA/PBS and DHS/FPS operate under a Memorandum of Agreement (MOA) for obtaining services, such as basic security for buildings, contract guards, law enforcement, background suitability determinations for contractors, including Child Care, and continuity of operations plan activation support.

The OIG remains concerned about the protection of federal buildings because of the shortcomings in FPS's ability to provide security that have been identified by the GAO and the availability of funding for building security measures. In FY 2009, GAO identified significant issues with FPS's ability to provide security, including weaknesses in the Contract Guard program and lack of a risk management framework to ensure the security of federal buildings and facilities. Further, a FY 2008 GAO report noted that FPS was experiencing difficulties in fully meeting its facility protection mission due to staffing and operational issues.

The availability of funding for security measures is also an issue. Under the existing MOA, security fixtures and mandatory security equipment countermeasures valued above the prospectus-level, or installed in prospectus-level projects, have been purchased and installed by GSA on a prioritized, funds available basis. PBS Regional Commissioners reserve the right not to implement mandatory measures, after consulting with DHS. With the exception of prospectus-level equipment or projects, security equipment determined by FPS to be a mandatory countermeasure is supposed to be funded by DHS or tenant agencies through Security Work Authorizations, on a prioritized, funds-available basis. FPS has been experiencing major funding shortfalls which could affect the availability of future funding for upgrades and replacement of the security countermeasure equipment initially authorized directly by Congress.

AGENCY ACTIONS: GSA formed a Security Division within the PBS Office of Facilities Management and Services Programs, including a Regional Security Network. The Security Division has taken an active role on Interagency Security Committee (ISC) working groups which have been addressing significant areas, such as revised standards for facility security level determinations and baseline standards for existing facilities. The agreement between GSA and FPS addressed the roles, responsibilities and operational relationships between FPS and GSA concerning the security of GSA-controlled space. Negotiation of a new MOA is presently on hold, pending the proposed shifting of FPS from the Immigration and Customs Enforcement bureau into the National Protection and Programs Directorate. The new MOA will have to take into account numerous areas, including ISC security standards, security equipment maintenance and the impact of FPS's policy change to transition to an inspector based workforce.

FEDERAL BUILDINGS FUND

ISSUE: Challenges Exist for Capital Projects and Long-Term Funding. PBS is one of the largest real property organizations in the world. Its building inventory consists of over 8,600 assets, mostly general purpose office space in federal buildings and leases, with almost 352 million square feet of rentable space, and housing over a million federal employees. Leased space accounts for approximately 51 percent of the portfolio. Real property operations are funded through the FBF. The FBF is a revolving fund in that rent collected by PBS is deposited into the fund. Those funds are then used to not only make lease payments and operate government-owned buildings, but also for investment in the capital program to repair and modernize facilities and construct new buildings within the limits set annually as part of the budget process. The buildings in PBS's owned portfolio have an average age of 46 years and require approximately $5 billion in reinvestment for repairs and alterations. The OIG is concerned that the recent influx of funding from the Recovery Act for capital projects introduces new risks. Further, while GSA devotes its attention to the Recovery Act projects, it is important that long-term funding issues still be addressed, since funding beyond FY 2009 may not meet GSA's needs to ensure that buildings are properly maintained.

Capital Projects

The Recovery Act will create an additional burden on GSA due to the volume of the funding and the short time frame for obligating the funds. GSA's capital program is typically funded at $1.3 billion annually and GSA's staffing is geared toward this level of funding. However, the Recovery Act increases construction funding to four times GSA's typical construction budget for a single year and requires GSA to obligate the majority of that funding in a 20-month period. This workload will strain GSA's capabilities as resources must be devoted to plan for new projects and acquisitions in a shortened timeframe. As resources are diverted to these projects, GSA's other construction work may be impacted by delays or rushed work.

Long-term Funding Issues

Until recently, the funding for capital projects had been decreasing. This funding decrease was exacerbated by increasing construction costs, which led to fewer projects at the same funding level. However, the funding situation changed in FY 2009. Through the Recovery Act, GSA received $1 billion for new federal buildings, courthouses and land ports of entry, as well as $4.5 billion to convert the GSA owned buildings to high performance green buildings.

To replenish the FBF and provide funds for the capital program, PBS will continue to rely on its operations. However, its net revenue has been falling. In FY 2005, PBS's net revenue was $974 million, but that fell to $551 million in FY 2008. Likewise, PBS's primary measure for tracking the incoming Funds From Operations (FFO), which is essentially net revenue before depreciation is deducted, or total revenue less all expenses except depreciation, has also dropped. PBS's FFO peaked in FY 2005 at $1.762 billion, and dropped to $1.623 billion in FY 2008. PBS's net revenue and FFO have been falling as operating costs for its owned buildings have increased faster than revenues. In addition, net revenue has also been impacted by PBS's leasing operations, which lost $25.5 million in FY 2007 and $68.7 million in FY 2008.

PBS's revenue and expense picture for the future is mixed. PBS rental rates for owned space are based on market appraisals that are set well in advance of taking affect, and leases are supposed to be priced so that they are revenue neutral, incurring neither a profit nor a loss. PBS revenue from owned space should increase as new buildings and renovated buildings are put into operation. However, the increase may be limited as the current market appraisals used to establish future rental rates are affected by the current economic downturn. Additionally, PBS's leasing revenue will be affected by the reduction of its leasing fee from eight percent to seven percent (from six to five percent for non-cancelable leases) that took effect in FY 2008.

Conversely, the rise in PBS's operating expenses should slow down. The current economic slowdown could help to slow the rise in operating costs, such as cleaning and maintenance, as competition in the current environment should lead to lower contract costs. Also, in the future, PBS could see its energy consumption reduced as it uses Recovery Act funds to take measures to convert its buildings to high performance green buildings. If these measures are effective, PBS's future energy consumption should be reduced, and the increases in its energy costs should slow or be reduced accordingly. However, until these measures are in place and operating, energy costs will likely continue to impact PBS.

The capital reinvestment needs of PBS's government–owned buildings have been growing. Without the necessary funding for reinvestment, buildings will continue to deteriorate, and as a result, rent prices would also be lower as the building conditions are reflected in the rent appraisals, leading to even lower revenue. Using leasing as a long-term solution may not be feasible, as lease operations are only expected to break even, and have recently been losing money.

AGENCY ACTIONS: To address this challenge, PBS is taking action in several different ways. To provide oversight to the Recovery Act work, PBS has established a program management office at the central office level, and put vehicles in place to obtain supplemental assistance in the conduct of the Recovery Act work. With regard to current assets, PBS is taking short term and long term steps. In the short term, PBS has requested $525 million in new appropriations in its FY 2010 budget request. These funds are needed to ensure PBS's capital program stays on plan in the near term. In the long term, PBS has implemented a portfolio strategy to maximize income-producing properties and identify underperforming assets. PBS has also adjusted its priorities to address these issues.

In FY 2007, the former PBS Commissioner also identified PBS's priority areas, several of which affect the capital program. His priorities include improving PBS's real property capital project planning and delivery. To achieve this, PBS is developing project monitoring and mitigation tracking tools, and establishing national program standards for ownership of project data accuracy. PBS is also executing a national training strategy and action plan for project managers, as well as developing future leadership in the Office of the Chief Architect. The primary goal of these efforts is to deliver projects on time, on budget and within scope.

PBS's priorities also include exploring ways to leverage funding of real property capital projects to help offset the growing burden of capital funds. PBS is examining increased investment in real property through the use of alternative financing options, as an opportunity to support further investment and reinvestment in its portfolio. To do this, PBS is seeking to use authorities identified under Section 412 of the FY 2005 appropriation law. Under this authority, PBS was given the authority to not only deposit proceeds from the disposal of GSA owned property into the FBF, but also the ability to out-lease GSA owned property and then lease it back. With these authorities, PBS would like to out-lease properties in need of reinvestment to an entity that would perform the needed repairs and alterations, and then leaseback the renovated property from that entity. Thus the reinvestment costs will be financed through a lease arrangement rather than being funded directly through the FBF.

PBS is also examining its leasing program results. It is working to identify leases with negative financial results and take steps to mitigate the losses. It is also working to address its lease extensions and holdovers that impact its leasing workload. PBS will also be working to find opportunities for reduced lease rates in the current economic environment and take advantage of these opportunities to reduce its leasing costs.